BEFORE THE
PUBLIC SERVICE COMMISSION OF WISCONSIN

Application of the Milwaukee Water Works
for Authority to Increase Water Rates — Docket 3720-WR-108

SURREBUTTAL TESTIMONY OF JOHN WRIGHT ON BEHALF OF MILWAUKEE WATER WORKS

Q. Please state your name and business address.

A. John J. Wright, 12385 East Arapahoe Road, Tower II, Suite 600, Centennial, CO, 80112.

Q. Have you previously filed direct and rebuttal testimony in this docket?

A. Yes.

Q. What is the purpose of you surrebuttal testimony?

A. My surrebuttal testimony will address certain portions of the rebuttal testimony filed by: Mr. Sam Shannon on behalf of the Public Service Commission of Wisconsin; Mr. Andrew Behm and Mr. Christopher Kaempfer on behalf of the Wholesale Customer Group; and Mr. Phillip Q. Hanser on behalf of MillerCoors.

Allocation of Public Fire Protection Costs to Wholesale Customers

Q. How do you respond Mr. Sam Shannon's agreement that wholesale customers should not be allocated public fire protection costs?

A. MWW agrees that if a wholesale customer receives no public fire protection benefit from the MWW system, it should not pay any public fire protection costs. However, before the Commission disallows the allocation of public fire protection costs to any specific

wholesale customer, it must carefully consider whether that customer receives (or does not receive) public fire protection benefits from the MWW system.

My rebuttal testimony (Rebuttal-MWW-Wright-5 to 8) offered a potential approach to making this determination based on the Commission's decision in the 2011 Oak Creek Water and Sewer Utility rate case (PSC REF#: 168775). In that testimony, I highlighted the many ways that the relationships between MWW and its wholesale customers differ from the factors that led to the Commission's decision in Oak Creek. Unless and until the Commission establishes that specific wholesale customers do not receive public fire protection benefits from the MWW system, it is premature to recommend the disallowance of public fire protection costs to wholesale customers.

Q. How do you respond to Mr. Shannon's criticisms of the population-based methodology used to estimate public fire flows?

A. Contrary to the impression that may be created by Mr. Shannon's rebuttal testimony (Rebuttal-Wholesale Customers-Shannon-4 to 5), MWW did not reach back to some dusty and obscure methodology devised by the Commission in the early 1900's to identify our proposed approach for determining public fire flows and allocating public fire protection costs. Instead, MWW used the *exact same approach* adopted by the Commission *just three years ago* in its final decision in MWW's 2009-11 rate case (PSC Ref#144469). This methodology was not only adopted by the Commission, but it was sponsored by then PSC staff witness Andrew Behm. Further, when the Commission adopted its final decision in the above referenced rate case, it felt comfortable enough with the use of population-based fire flow estimates to deny a recommendation by Mr.

Behm that MWW's maximum public fire flow demand be lowered from 19,440,000 gallons to 12,960,000 gallons.

Q. Shouldn't members of the PSC staff have the option of changing their position on technical and public policy issues over time?

A. Every stakeholder to the regulatory process should have the opportunity to modify their position over time based on a reasoned analysis. Nonetheless, as a former staff member at both the Colorado Public Utilities Commission and the Oregon Public Utility Commission, I would suggest that regulatory consistency, equally applied across all regulated utilities, is an important goal that every regulatory agency should strive for. From my perspective, the public fire protection testimony offered by Mr. Shannon does not demonstrate such consistency.

Q. In what way does Mr. Shannon, and by extension, the PSC Staff, fail to demonstrate regulatory consistency as it relates to public fire protection.

A. Mr. Shannon has rejected two key portions of the public fire protection methodology adopted by the Commission just three years ago in Docket No. 3720-WR-107. First, he rejected the use of a population-based methodology to estimate public fire flows. In this regard, I would simply note that on July 31, 2013, the Commission issued its Final Decision (PSC Ref#: 188160) in the Kenosha Water Utility (Kenosha) rate case (Docket No. 2820-WR-106). In Schedule 4 of the Commission-adopted cost of service study, the volume of public fire flows assumed for Kenosha are 2,940,000 gallons (7,000 gallons per minute for a duration of seven hours). Kenosha has a population of approximately 100,000 and the Commission-adopted public fire flow of 2,940,000 gallons very closely approximates the amount that would be calculated using the population-based formulaic

approach adopted by the Commission in Docket No. 3720-WR-07 and proposed by MWW in its cost of service study (3,020,340 gallons for a population of 100,000).

The important point to note is that the Commission-adopted cost of service study for Kenosha did not utilize the Insurance Services Office ("ISO") "Basic Fire Flow" of 3,500 gallons per minute for a duration of four hours as discussed in Rebuttal-PSC-Shannon-2 to 3. Nor did the Commission-adopted cost of service study for Kenosha assume public fire flows of 3,000 gallons per minute for a duration of three hours - a metric so frequently referenced in the rebuttal testimony of Mr. Christopher Kaempfer submitted on behalf of the Wholesale Customer Group. This raises the obvious question regarding regulatory consistency on the part of the PSC staff. If a public fire flow volume of 2,940,000 gallons was acceptable in the Kenosha rate case just eleven months ago, why are similarly calculated volumes so unacceptable when used by MWW in its cost of service study?

Mr. Shannon has also rejected a second key aspect of the Commission-adopted cost of service study in MWW's 2009-11 rate case. That is, he has rejected the allocation of public fire protection costs to wholesale customers. As discussed in his rebuttal testimony, Mr. Shannon indicates that MWW's wholesale customers "seem" to have offered a reasonable justification for not being assessed a public fire protection charge because they have their own distribution storage capacity to fight fires (Rebuttal-Wholesale Customers-Shannon-2). This is not the test imposed by the Commission on the Village of Pleasant Prairie (Pleasant Prairie) in the Kenosha rate case. In that case, the Commission explicitly rejected Pleasant Prairie's request to avoid the assessment of Kenosha public fire protection charges because Pleasant Prairie could not demonstrate

that it had adequate storage to meet its combined maximum day demands plus fire flow. As noted in my rebuttal testimony, this was also a key test considered by the Commission in the 2011 Oak Creek Water and Sewer Utility rate case (Docket No. 4310-WR-104).

This raises the obvious question regarding regulatory consistency on the part of the PSC staff. If the ability of a wholesale customer to meet public fire flow demands under maximum day load conditions was a critical factor in both the 2013 Kenosha rate case and the 2011 Oak Creek rate case, why is it not mentioned as a key factor in Mr. Shannon's analysis of whether MWW's wholesale customers have adequate storage facilities?

Q. What request would you make of the Commission regarding public fire protection issues?

A. MWW respects the Commission's regulatory authority and the capabilities of the PSC staff. This is why MWW made only two significant changes to the PSC staff-prepared cost of service study adopted by the Commission in MWW's 2009-11 rate case (customer class demand factors and water main allocations to the transmission and distribution functions). Nonetheless, the uncertainties regarding key public fire protection issues coupled with fluctuating positions on the part of the PSC staff make very difficult for MWW, and by extension, any Wisconsin water utility offering wholesale public fire protection services, to have any certainty in rate case proceedings regarding the estimation of public fire flows and the allocation of public fire protection costs.

MWW urges the Commission to provide definitive guidance regarding a range of public fire protection issues noted below. We also urge the PSC staff to apply this

guidance in a consistent method across all Wisconsin water utilities. The required guidance includes:

1. How should public fire flows be estimated? For example, should ISO guidelines be used or the long-established Commission precedent of using population-based estimates?
2. What circumstances should cause public fire protection charges to be assessed to wholesale customers? For example, is any level of wholesale customer storage adequate or must wholesale customer storage be definitively demonstrated as adequate to meet maximum day demands plus public fire flows?
3. What is the appropriate methodology for allocating public fire protection costs to customer classes? For example, should each customer's proportionate share of total estimated public fire flows or the equivalent meter method used in the Kenosha rate case and referenced in Mr. Shannon's rebuttal testimony be used?

Q. What are your comments on Mr. Shannon's rebuttal testimony regarding the cost of service ramifications of disallowing the allocation of public fire protection costs to wholesale customers?

A. I find Mr. Shannon's testimony to be thoughtful in this regard but I have not had the opportunity to verify the dollar amounts he references. Unless and until the Commission renders a final decision disallowing the allocation of public fire protection costs to some or all of MWW's wholesale customers, we have no intention of entertaining any proposals that do not include the allocation of public fire protection costs to wholesale customers.

Q. What is MWW's bottom-line position regarding the allocation of public fire protection costs to its wholesale customers?

A. As noted above, MWW agrees that if a wholesale customer receives no public fire protection benefit from the MWW system it should not pay any public fire protection costs. Mr. Kaempfer (Direct-Wholesale Customers-Kaempfer-1 to 5), testifying on behalf of the Wholesale Customer Group, has recommended eliminating or reducing the public fire protection charges allocated to the following MWW wholesale customers: the Village of Brown Deer, the Village of Butler, the Village of Greendale, the Village of Menomonee Falls, the City of New Berlin, the City of Wauwatosa, the City of West Allis, and the City of Mequon.

Based on the tests considered by the Commission in the Oak Creek and Kenosha rate cases, MWW believes that Mr. Kaempfer has not made an adequate showing that the MWW system provides no public fire protection benefit to these customers. Therefore, we urge the Commission to approve the allocation of public fire protection costs to wholesale customers as proposed in MWW's cost of service study.

Rate of Return Differential for Retail and Wholesale Customers

Q. How do you respond to Mr. Behm's argument that water sales to wholesale customers do not increase the risk of sales variability?

A. Mr. Behm's rebuttal testimony regarding the variability of wholesale versus retail water sales revenue is a proverbial red herring that has virtually zero applicability to the question of whether there should be a 100 basis differential between the retail and wholesale customer rates of return on rate base as requested by MWW.

The salient issue is most definitely not climate or business cycle induced water sales revenue variability. Instead, it is whether wholesale customers have the potential to leave the MWW system and thus subject MWW to a significant loss of revenue and potentially stranded infrastructure. According to MWW's 2013 PSC Annual Report, MWW sold 7.4486 billion gallons of water to wholesale customers in 2013 and had wholesale water sales revenues of $9.39 million (Ex.-MWW-Wright-10, p W-3). MWW sold 30.560 billion gallons of water to retail customers in 2013 and retail water sales of $77.38 million (Ex-MWW-Wright-10, p W-2). Thus, wholesale customers accounted for approximately 19.60% of MWW's total water sales by volume and approximately 10.83% of MWW's total water sales revenue. These are not trivial rounding errors and MWW's contracts with its wholesale customers are not perpetual in nature. The loss of even a portion of its existing wholesale customer demand would have significant negative impacts on MWW's finances and the water rates of retail customers. This is indeed a legitimate risk borne by the urban retail customer/owners of MWW's system and one for which they should receive compensation via a 100 basis point rate of return differential.

Q. Mr. Behm claims that you have characterized the 100 basis point differential as a "dividend" to retail customers. Do you agree?

A. This is yet another misleading argument on the part of Mr. Behm. Nowhere in my direct or rebuttal testimony have I used the word "dividend" to describe MWW's rationale for a 100 basis point rate or return differential. Instead, I have made it clear that the urban retail customer/owners of MWW should be compensated for the very real and legitimate risks incurred by MWW to provide wholesale service.

The Commission found reasonable a 100 basis point differential in MWW's last rate case (PSC REF#:144469, p. 9). PSC staff witness Anne Waymouth testified about the Commission's historical guidelines for approving differential rates of return and the AWWA M1 Manual's discussion of the justifications for differential rates of return. (Direct-PSC-Waymouth-9 to 10). Finally, as noted in both my direct and rebuttal testimony, the use of a basis point differential of the type requested by MWW has long been accepted by the American Water Works Association.

Q. Do you have any additional comments regarding the rate of return differential?

A. Although he did not testify on the matter directly in MWW's 2009-11 rate case, Mr. Behm sponsored the Commission-adopted cost of service study that featured a 100 basis point differential similar to that proposed by MWW in this docket. Thus, like his testimony on the allocation of public fire protection costs to wholesale customers, Mr. Behm has taken a position in this proceeding that is contrary to the position he took in MWW's 2009-11 rate case while serving as a member of the PSC staff.

Allocation of Water Mains to the Transmission and Distribution Functions

Q. Do you have any comments regarding the rebuttal testimony of MillerCoors witness Mr. Phillip Q. Hanser regarding the allocation of water mains?

A. I concur with Mr. Hanser's rebuttal testimony. MWW believes that that the cost of repairing and replacing its water mains is proportional to the size of the main as expressed by the metric inch-feet. MWW acknowledges that the use of inch-feet to allocate the value of MWW's water mains between the transmission and distribution functions results in a higher level of costs being shifted to wholesale customers. This outcome notwithstanding, MWW believes that inch-feet is provides a more equitable

basis of allocation. This was basis of allocation previously used by the Commission for MWW until changed by Mr. Behm in MWW's 2009-11 rate case.

Q. How do you respond to Mr. Hanser's contention that MWW is inappropriately allocating the cost of small distribution mains to large industrial customers?

A. Mr. Hanser has offered testimony arguing that large retail industrial customers such as MillerCoors are served by large meters and thus make no use of smaller sized mains on the MWW distribution system (for example, MillerCoors is served by an 8" meter). He notes that MWW's wholesale customers are served by meters of size between 6" and 12" in diameter but, unlike large retail industrial customers pay no share of MWW distribution system costs. As I understand it, Mr. Hanser's desired outcome is that large retail industrial customers should only be allocated costs for that portion of the distribution system he argues they utilize.

This issue was also raised by MillerCoors in Docket No. 3720-WR-107 and was the subject of extensive testimony. For example, see the rebuttal testimony of Mr. Andrew Behm on behalf of the PSC staff (Ex.-MWW-Wright-11, R12.8 to 9) and the direct testimony of Mr. Michael Gorman on behalf of MillerCoors (Ex.-MWW-Wright-12, D13.14 to 16). Ultimately, the Commission's Final Decision (PSC Ref#: 144469) on this issue was as follows:

> The record indicates MillerCoors is served by an 8-inch water meter. According to MillerCoors, it must be served through at least an 8-inch main, and it does not receive any benefit from smaller distribution mains. MillerCoors proposed that none of the cost of these distribution mains smaller than 8 inches be allocated to it. Its proposal would establish a separate large-industrial customer class, of which MillerCoors would be a member.
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> Commission staff countered that large customers such as MillerCoors do receive a benefit from 6-inch distribution mains,

even if they receive primary, everyday service through larger mains. It stated that smaller mains play a supporting role in the distribution system by providing system redundancy and backup supply to large customers.

Commission staff also maintained that, although industrial customers are not all identical, their demand patterns are similar enough to justify aggregating them in one customer class.

Costs are assigned based on the average characteristics of the class rather than the specific characteristics of individual customers.

The Commission finds that large customers receive at least an indirect benefit from smaller distribution mains. It also concludes that separating customers based on size would add to the complexity of the COSS without significantly improving its accuracy or fairness.

Q. Does MWW continue to support the Commission's Final Decision in Docket No. 3720-WR-107 regarding small diameter mains?

A. Yes. MWW continues to believe that large retail industrial customers receive at least some benefit from small diameter mains on the MWW distribution system. Therefore, we do not recommend a modification of our proposed cost of service methodology to address Mr. Hanser's issue.

Q. Does this conclude your surrebuttal testimony?

A. Yes.